1933

Economic Conditions
Governmental Finance
United States Securities

New York, July, 1933.

General Business Conditions

THE upward movement of business has continued during June without interruption. At this time of the year business men usually expect a Summer recession to be well under way, but this rise is so vigorous that seasonal restraining influences thus far have had no effect. Operations have been stepped up steadily in the industries, and despite the increases in output and shipments their unfilled orders are holding at very satisfactory levels. In most lines the backlog is sufficient to keep mills and factories going for some time, and little is now heard of the expectations of a substantial Summer decline, which were entertained in many quarters a month or more ago. On the contrary, as the season advances with the news continuing good the time in which a recession might be looked for is correspondingly shortened. Within a few more weeks the crops will be moving, and considering the improved farm prices there is reason to hope that the Fall rise in trade will be a substantial one, bolstered by a greater farm purchasing power than has been present in the past year or two.

Stock prices have advanced since the first of March by some 85 per cent and bond prices by 15 per cent, according to representative averages. The recovery in the value of the stocks and bonds listed on the New York Stock Exchange up to June 1 was fifteen billions of dollars. This is much more than a sentimental influence on business. It has added to purchasing power not only because some of the profits have been realized, but because the rise increases the ability of security owners to command credit.

Over the three months since the improvement began industrial activity shows an unbroken expansion. With the exception of construction work and lines particularly dependent upon construction and equipment, operations are generally the highest in about two years, and in some industries, notably the textiles, it is necessary to go back into the boom period to find the comparison. The following table gives the record of steel mill operations, car loadings, and electric power production, three of the recognized measures of business activity, since the middle of March. The figures show the steady rise both from week to week and by comparison with the corresponding weeks one year ago:

Week Ended		Steel Mill Operations % of Capacity	Steel Mill Operations % Change from 1932	Car Loadings Thousand Cars	Car Loadings % Change from 1932	Elec. Pow. Production Mill. Kw. Hours	Elec. Pow. Production % Change from 1932
Mar.	18	15	— 40.0	450	—23.1	1,375	—10.6
"	25	14	— 44.0	476	—15.1	1,410	— 6.9
Apr.	1	15	— 31.8	495	— 9.2	1,402	— 5.3
"	8	16½	— 25.0	487	—10.6	1,399	— 4.5
"	15	19½	— 7.1	494	—12.8	1,410	— 4.8
"	22	23	+ 2.2	493	—12.3	1,431	— 2.6
"	29	25	+ 8.6	536	— 3.3	1,428	— 1.8
May	6	29	+ 20.8	524	— 1.8	1,436	+ .5
"	13	31	+ 29.1	531	+ 2.6	1,468	+ 2.1
"	20	35	+ 40.0	532	+ 3.1	1,483	+ 3.3
"	27	38	+ 58.3	541	+ 3.8	1,494	+ 4.8
June	3	41	+ 78.2	508	+13.5	1,462	+ 5.9
"	10	44	+120.0	565	+12.5	1,542	+ 7.4
"	17	47	+161.1	588	+13.4	1,578	+ 9.5
"	24	50	+212.5			1,598	+10.9
July	1	53	+253.3				

Rise Exceeds All Previous Records

This is the most impressive showing of business recovery ever made in a comparable period in this country. Of course these increases in production and trade are generating purchasing power at an encouraging rate. The industries are giving more employment and in many cases at better wages. From April to May there was an increase of 5 per cent in factory employment and of 11 per cent in payrolls, according to the Department of Labor, and these figures contrast with the usual seasonal movement, which is downward. During June further increases undoubtedly have occurred, and according to published estimates by the American Federation of Labor more than 1,600,000 workers have been re-employed since the end of March.

Moreover, the changes affecting the various classes of the population have been on the whole in the direction of a better business equilibrium, due to the agricultural improvement. The farmer is gaining not only because the prices of his products are better, but because they have advanced more than the prices of the things he buys. According to the latest

92

price index numbers of the Bureau of Labor Statistics the farm products group was up 30 per cent from the low and the foods group 14 per cent, while all other groups combined were only 3 per cent higher. Between March and May the ratio of the prices the farmer receives to the prices he pays rose from 50 to 62 per cent of the pre-war average, according to the Department of Agriculture's calculations, and doubtless it has risen further since. The figure shows that there is still a long way to go, but this is the most encouraging movement since the depression began toward establishing a more equitable price relationship that will restore trade between the farm and industrial populations.

Impressed by these gains, business men are looking forward to the second half-year with confidence. They recognize the elements of confusion in the economic situation and the untried character of the program under which they are operating; and doubtless these uncertainties will continue to restrict capital investment and the undertaking of projects for the future. As related to current operations, however, the chief consideration is that the turn has been made, both in business volume and prices, and forward buying is again the favored policy.

Gains in Industrial Activity

The table on the preceding page shows that the steel industry has held its leadership in the upward movement, with operations up to 53 per cent of capacity, according to the most recent estimate of the Iron Age. This is the highest figure since the Spring of 1931, and is but a few points less than the rate in the Summer of 1930. At the rate of the past few weeks this important industry can show a balance on the credit side of the ledger, after two years of operating deficits.

A striking feature of the steel reports is that some mills have had difficulty in keeping up with deliveries. The explanation is that mills have been unwilling to give contracts for third quarter delivery without stipulations to protect themselves against increased production costs; and therefore buyers have taken all the steel they could get at the advantageous second-quarter prices. This rush of shipments may suggest some falling off later on, but the opportunities for speculative buying have been limited, and the amount of steel delivered during June which will not go into immediate consumption is small. The steel makers take a very confident view of the prospect, looking ahead to the time when construction and railway requirements will add to the demand, which thus far has come from the automobile and can manufacturers and from the great variety of miscellaneous users.

The automobile business gives a direct indication of consumer buying power, and the showing is the best in nearly two years. May production, which was closely adjusted to sales, totaled 218,171 vehicles, the highest since July, 1931. Contrary to the usual trend, June is expected to show an increase over May, and the latest reports still give no evidence of the expected seasonal slackening of sales. Tire business has been very heavy, with two price advances in five weeks and factories running on seven-day schedules.

Construction activity is still too low to give much support to business, but the latest figures for this major industry, whose operations from the peak in 1928 to the low point of this year suffered a drop of more than 90 per cent, are more encouraging than in a long time. Daily average awards of contracts during the first twenty-two days of June, as reported by the Dodge Corporation, were but 1.2 per cent less than during the month of June, 1932, and in residential building they were 22.4 per cent greater. The rise has been pronounced since the first of May though usually awards decline at this season. This gain is without benefit of the public works program, but the provision of the Industrial Recovery Act authorizing the expenditure of $3,300,000,000 is expected to result in a marked expansion in this class of work in the near future. Many of these projects are ready to go ahead as soon as the necessary approval by Federal and local governments is obtained, and a summary of those which are ready for construction as compiled by the Engineering News Record reaches the impressive total of 3,446 individual projects with an estimated cost aggregating $2,617,848,250.

Textile Mills Sold Well Ahead

Cotton mills in May ran at the highest rate since the Fall of 1929, and a further expansion has occurred in June which has lifted operations to, or close to, an all-time high record for the month. Demand for cotton mill machinery is reported the best since 1920. The inducement to build up stocks and cover forward requirements of cotton goods has been almost continuous, for in addition to the rise in raw cotton the effect of the general economic program is to increase manufacturing costs heavily, and of course the increased cost must be recovered in the price. Wages will be raised and mill operations arbitrarily reduced by the middle of July, under the Industrial Recovery Act, and a processing tax is about to be levied under the Farm Relief Act. The rise in the manufacturing margin in print cloths from 7.84 cents per pound on March 31 to 18.48 cents on June 16, according to the New York Cotton Exchange Service's calculations, tells the story. During June the goods

markets have been quieter, and after nearly three months of exceptional activity this is a healthy development, giving time for the markets to adjust themselves to the new conditions with less danger of a setback.

Fall clothing business has been excellent, and manufacturers have booked large advance orders for the first time in several years. Woolen goods markets have been correspondingly active, prices have advanced sharply, and with orders on hand for two months' output mills have stepped up operations to as near capacity as is practicable. Rayon prices are up again, with both yarn producers and cloth mills sold well ahead. Shoe production in May topped the previous record for the month, made in 1929, according to preliminary estimates.

Coal production is running well above last year, and lumber orders are the best in two and a half years. Chemical, glass, furniture and paints have shared the upturn, and in fact there is no industry from which the reports are not substantially better.

Retail trade has shown general gains. Early figures indicate that department stores sold approximately as much, in dollars, in the first part of June as they did a year ago, when prices were 8.4 per cent higher, according to the Fairchild index. These figures indicate that a substantially larger volume of merchandise has moved across the counters, and the chain stores give similar reports.

Prices and Speculation

If there is anything in this impressive picture of advancing business to raise a question as to the continuance of the improvement it relates to the nature of the price advance and the influence of the speculative buying, and this has become the topic of chief interest to business. The price rise has continued during June, though some of the staples which led the May rise have reacted. However, the grains have set new highs on the reports of damage by the heat wave, cotton has advanced in response to the acreage reduction program, and no important signs of weakness have appeared anywhere. Naturally prices of manufactured goods are joining the advance, both at wholesale and retail.

There is no reason for alarm merely because prices have advanced rapidly. The recovery was inevitable, and it is natural that it should be rapid in view of the abnormally depressed levels to which prices had fallen. From the Autumn of 1931 the banking situation in this country exerted a destructive pressure on prices, and when the banking crisis brought the climax of this deflation, and the pressure eased, the rebound was natural. All economists have been of the opinion that prices would recover as business recovered, in view of the experience of past depressions and the abundant credit resources to support a higher price level, and this is what has occurred.

It is a misinterpretation of the situation to assume that the depreciation of the dollar in the foreign exchanges has been principally responsible for the price advance. Sentimentally it has had an important influence, since it measures the expectation of inflation; but its direct effect is very limited. The change in the value of the dollar abroad affects its value at home only as the prices of imported and exported commodities are affected. Naturally imported goods such as rubber, silk, tin, cocoa and others move higher in dollars, if the price is unchanged in the country of origin, but the goods this country offers for export will rise only in case the cheapening of the dollar attracts a greater demand for them.

There is no evidence that this has been the case to any important extent. Exports of cotton have increased, but as the price of cotton has risen in European currencies as well as in dollars evidently another factor than the cheapness of the dollar is at work, and that factor is the business improvement abroad as well as here. The price of wheat has not been directly affected, since this country is not exporting wheat, our prices being above the competitive prices in the world markets. Our corn and oats are not exported, and our general export trade has apparently not been stimulated. In May exports showed a moderate increase of 8 per cent over April in value of exports, reflecting principally the price advance, while imports show the larger increase of 21 per cent, and this indicates an increase in the volume also.

Rise in Prices Abroad

Moreover, the staple commodities which have risen in price here have advanced in other countries also, though in less degree. Tin since the end of April has risen in London from £164 per ton to £225; copper from £35 to £41; rubber from $2\frac{9}{32}$ pence per pound to $3\frac{1}{2}$. Silk is up in Yokohama from 800 to 1000 yen per picul bale; cotton in Liverpool from 5.52 pence to 6.53. The Federal Reserve Board has made a study of the price of six staples important in international trade which shows that between February and the end of May they rose 30 per cent in British sterling quotations, and 60 per cent in this country. This rise in British prices, which has been independent of currency fluctuations inasmuch as the gold value of sterling showed little variation between the dates given, is evidence of the genuine basis for the improvement, derived from the low stocks of manufactured goods, reduced surpluses of raw materials, and improved demand.

Manifestly the natural rise in prices that has occurred is a cause for the greatest satisfaction. It confirms the opinion that the chief cause of the fall was the disorder in production and exchange, the banking difficulties and the loss of confidence, all interacting in the manner of a vicious circle; and that neither the money supply nor the monetary system was an important factor in it. No increase in the circulation was necessary to make the turn, for the supply is no larger than at the bottom of the depression a year ago, and is diminishing.

There is no reason to doubt that the business activity will continue without additions to the supply of money, provided the normal tendency to recover the equilibrium is not disturbed. Hence the degree in which the Government, pursuing the price-raising program, may find it necessary to use its inflationary powers is being diminished as the improvement goes on; and since the hazards of inflation are in proportion to the degree in which it is used this is a very reassuring development.

The speculative buying that is going on does not of itself endanger the prospect for continuing recovery, but will do so if it is ill-judged and drives the markets too high. We called attention last month to the economic service of intelligent speculation, such as experienced business men undertake in covering their forward needs. It gives the start to recovery, gives the producers the benefit of the improvement at an early stage, and assists in the prompt distribution of the new purchasing power. But the danger that it may run away, in view of the promise of higher prices that is being held out, is one that should be guarded against by all concerned.

The events of the past month, and particularly the minor "stabilization crisis" that occurred upon the reports of negotiations to fix the relationship between the dollar and the pound, demonstrate the chief difficulty in attempting a program of inflation, which is that a continuous or repeated application of the stimulus may be necessary to maintain its effects. They give a lesson of the wisdom and restraint that is necessary not only to keep the program within moderate bounds, as intended, but to harmonize it with other policies recognized by economists as essential to the restoration of prosperity, including the restoration of a common standard of value among the nations and the avoidance of anything resembling a competitive depreciation of currencies.

Money and Banking

The supply of funds in the money market has continued plentiful during the month. Over the country as a whole the banks have had a larger excess of reserves above requirements than in May, though this has not been the case in New York City, due to a shifting of funds to the interior. The excess funds have come principally from the return of currency out of hoarding, which in the first three weeks of the month resulted in a reduction of $114,000,000 in money in circulation. In the same period the Reserve Banks purchased $65,000,000 of U. S. Government securities, which put a corresponding amount of Reserve Bank credit in the market. Out of these funds the member banks paid off $80,000,000 of rediscounts, reducing them to $222,000,000, the lowest figure since the Summer of 1931. The remaining funds went principally into building up the member bank reserve balances, which in the middle of the month rose to the highest total since early February.

On the demand side of the market secured loans have shown a moderate expansion, those of the reporting member banks having increased $56,000,000 in the first three weeks of June. Inasmuch as brokers and security dealers in New York City increased their borrowings by $138,000,000 in the same period it is evident that some liquidation of secured loans by other customers of the banks occurred. There is still no evidence of any general increase in commercial borrowing. The item of "all other" loans for the reporting banks decreased $41,000,000 in the three weeks, and the total is but $180,000,000 above the low point made during the banking holiday.

The banks have increased their investments, but wholly in the United States Government securities portfolio. Most of this increase occurred in the week ended June 21, when there was a rise of $317,000,000 and is accounted for by subscriptions to the Treasury notes and certificates offered on June 15. As a rule increases in holdings of Governments on the date of such subscriptions are but a step in the distribution of the new offering, the tendency being for the figures to fall in the following weeks.

With demand for funds continuing light, as the foregoing figures show, and the outlook favoring a continuing addition to reserves through the return of currency and the Reserve Banks' open market operations, rates have continued easy. At the beginning of the month the rate on bankers' acceptances was reduced to 3/8 of 1 per cent asked for 90-day bills, and commercial paper offered in the open market has eased to 1½-1¾ for best names.

The Banking Act of 1933

The Glass-Steagall banking act, whose formal title is given above, was passed by Congress on the last day of the session and makes a large number of fundamental changes in the banking statutes. It deals with most of the

criticisms of the banking system that were raised during the boom and after, and responds to them by increasing the responsibility of the Government for the operation of the system. The new act is a very lengthy document and we have space to give only a few of the more important provisions, but they will indicate its general direction and intent.

Undoubtedly the chief of the changes is the provision for the insurance of bank deposits. For this purpose a corporation is set up whose stock shall be subscribed to by the Treasury in the amount of $150,000,000, by the Federal Reserve Banks in an amount equal to one-half of their surplus, also about $150,000,000, and by member and non-member banks (certified to be solvent) at the rate of ½ of 1 per cent of deposits. During the six months beginning January 1 next a temporary fund will be in operation, insuring in full deposits up to $2,500. Effective July 1, 1934 deposits up to $10,000 will be insured in full, amounts in excess of that and up to $50,000 at the rate of 75 per cent, and all above $50,000 at 50 per cent. Provision is made for assessment against the stockholder banks in the event of depletion of the fund. After July 1, 1936, all stockholder banks must be members of the Federal Reserve System.

The establishment of deposit guarantees or insurance in this country has always been regarded with apprehension, in view of the failure of the system in eight States where it has been tried. The fundamental objection to the plan is that it makes good bankers responsible for the losses of the poor ones, and naturally this is more likely to eliminate the former than the latter. It makes all banks equally safe for depositors and hence relieves the public of responsibility in the choice of banks. Thus it puts the burden of maintaining sound banking upon regulation by the Government, and takes it off the public, which should bear part of it.

The element of character in the choice of a bank is eliminated, and the competitive appeal is shifted to other and lower standards, such as liberality in making loans. The natural result is that the standards of management are lowered, bankers may take greater risks for the sake of larger profits, and the economic loss which accompanies bad bank management increases. All the arguments for the system are based upon the assumption that there will be no increase of bank failures because of it, and this assumption is fallacious.

In common with the original Glass bill, the chief aim of which was to put limits upon the use of member bank credit in financing speculative transactions, the new act for that purpose increases the powers of the Federal Reserve Board over the member banks. It authorizes the Board to withhold Reserve Bank credit from a bank when undue speculative use is made of its funds, and to fix the percentage of a bank's capital and surplus which may be represented by loans secured by stock and bond collateral; and if a bank borrowing from its Reserve Bank shall increase its loans on such collateral after official warning to the contrary its obligations to the Reserve Banks become immediately due and payable. The Board for cause may remove officers and directors of member banks from office.

Likewise the act requires the divorce by member banks of their security affiliates within one year, and prohibits any person or institution engaged principally in a security business from receiving deposits.

The act extends to national banks whatever branch banking privileges may be enjoyed by State banks within the same State, provided that no bank with a capital less than $500,000 may establish a branch outside of its own city.

Elimination of Interest on Demand Deposits

The enactment in the new Banking Act of a prohibition against payment of interest by member banks on demand deposits, effective on June 16 last, constitutes an important change of banking practice in this country, which has already taken effect in a pronounced shifting about in bank deposits and short term investments since that date. During the week ended June 21 the New York City banks showed a loss of $347,000,000 in net demand deposits. A substantial part of this loss was due to income tax payments and to cash purchases of the Treasury issues on June 15 and was offset by an increase in Government deposits out of the proceeds of the new issues; and another part represented a transfer from demand to time deposits, which increased $65,000,000. These offsets, however, leave a considerable loss to be accounted for, and withdrawals caused by the elimination of interest payments are the chief factor. Part of the funds withdrawn were placed in the call money market, where loans for account of out-of-town banks rose $27,000,000 in the week.

This prohibition like many others is a consequence of the abuse of a practice rather than of inherent unsoundness. In places where an excessive competition to obtain deposits existed during the boom period the rate paid was employed as a weapon in this competition, and the effect has been to raise rates to a figure which the banks could not pay except by investing their funds in securities of high yield. Naturally this practice increased the risks assumed in the investment portfolios, in making loans, and particularly in real estate obligations. The resulting losses, together with the

intent to reduce bank expenses as an offset to the cost of insuring deposits, give the explanation for including this prohibition in the act.

It will of course be some time before the permanent effects of the new law become known. To the extent that demand deposits are shifted into time deposits, or from one bank to another, there will be no change in total deposits of the banking system as a whole. But the elimination of all interest on demand deposits may induce many banks, industrial corporations and others who have been accustomed to carry large cash balances in the money centers to shift a portion of their funds into U. S. Government and other securities; and if deposits are contracted banks will find it necessary, other things being equal, to contract their investments and loans, the practical effect being to transfer bank investments into private hands. This may appear to be merely a shifting of funds, but may have unintended consequences.

Credits Outside the Banking System

At present the rates on short-term Governments, which doubtless would be favored investments for depositors making such shifts, are so low that the shift is not encouraged. However, the time may come when rates will induce greater transfers. Thus over a period of time there may be built up a body of short-term credits, invested principally in Government securities, outside of the regular banking system; and neither protected by banking reserves nor subject to control by the banking authorities. Like the call loans that were made in 1928 and 1929 by lenders other than banks and were a major factor in financing the stock market boom, but which at the first sign of trouble were hastily called for payment, the funds that may be diverted from bank deposits into short-term investments are strictly "fair weather money". When they are needed by the owners the investments will have to be sold, and if a large number of individual lenders, who do not have any responsibility for the money market, such as bankers and banking systems are expected to have, should decide to withdraw their funds at the same time, a shock to the securities market would be inevitable. Moreover, when these outside funds are thrown back into the banking structure, by having the banks purchase the investments and credit their deposit liabilities, it is necessary that they have or else borrow the additional reserves required to be kept against deposits, which would put an added strain on the banking system at the worst possible time.

The new laws regarding interest payments do not affect the deposits of mutual savings banks or of State and local Governments, or deposits in foreign branches. They apply only to banks which are members of the Federal Reserve System. State banks which are not members of the System may pay any rate of interest which they desire except as they may be restricted by their local banking authorities or by clearing house regulations, and this puts member banks at a disadvantage, which was likely not the intent of the Act. However, the provision that all banks admitted to the deposit insurance corporation must become member banks by July 1, 1936, will tend to unify the system, and to put all banks on the same footing.

Under the Act the Federal Reserve Board is directed to limit by regulation from time to time the rate of interest which may be paid by member banks on time deposits. Such regulations have not yet been issued. Meanwhile the rate on time deposits, other than thrift deposits, paid by the Clearing House banks of New York City has been set at ¼ of 1 per cent. Deposits payable in less than 60 days are classified as demand deposits.

The London Conference

The June issue of this Letter gave a discussion of the origin and purposes of the World Monetary and Economic Conference which is now in session in London, and since the Conference is still in the stage of negotiation nothing of a definitive character can yet be added to that discussion. The delegates naturally bring differing viewpoints to the council table, and since their views represent the aspirations of entire nations the task of reconciling the differences is a formidable one. Although the delegates are able to agree quite readily upon such general objectives as the re-establishment of the international gold standard, abolition of exchange controls and modification of the extreme restrictions upon trade, they evidently are not ready for immediate action along either of these lines. Each proposal raised is intricately related to other proposals, and the need to make a harmonious settlement of all prolongs the deliberations.

The Currency Stabilization Proposals

The most important cleavage in the Conference is upon the question of a temporary or de facto stabilization of the currencies of countries off the gold standard. Coincident with the start of the Conference, conversations upon proposals to stabilize the dollar and the pound sterling in relation to each other and to the franc were begun among representatives of the Treasuries and central banks of the United States, Great Britain and France. The United States gave official consideration to the proposals by sending the Treasury advisor, Dr. O. M. W. Sprague, to take part. Out of these deliberations came a provisional plan for de facto stabilization the precise nature

of which is only a matter of report, but which was transmitted to the respective Governments.

However, events in the United States made any proposals for stabilization at that time unwelcome to the Administration, which has declared its firm intention to raise prices, and has equipped itself with broad monetary powers for use if necessary to that end. Since the use of these monetary powers will tend to depress the dollar in the exchanges, the time obviously might come when policies of raising prices on the one hand, and of maintaining the dollar at a fixed value on the other, would become incompatible. While the proposals were up for discussion the markets were reactionary, and doubtless this fact influenced the decision to reject them.

The view of the United States was set forth in an official statement by the delegation on June 22, and is as follows:

Undue emphasis has been placed upon consideration of a plan proposed for temporary de facto stabilization of currencies. * * * * The American Government at Washington finds that measures for temporary stabilization now would be untimely.

The reason why it is considered untimely is because the American Government feels that its efforts to raise prices are the most important contribution it can make and that anything that would interfere with those efforts and possibly cause a violent price recession would harm the Conference more than the lack of an immediate agreement for temporary stabilization.

As to the ultimate objective, the American delegation has already introduced a resolution designed for ultimate world-wide stabilization of unstable currencies, and is devoting itself to the support of measures for the establishment of a co-ordinated monetary and fiscal policy to be pursued by the various nations in co-operation with the others for the purpose of stimulating economic activity and improving prices.

The French and British Views

This statement defines the American policy as one relegating stabilization to a subordinate position for the present, and putting the emphasis upon stimulating economic activity and advancing prices; and it places the United States and France in opposition upon the question. It is the French view that stabilization is an indispensable preliminary to other recovery measures, the argument being that there is no firm basis for such measures as long as currencies are free to fluctuate, to disturb trade, and to be used by one nation for trade advantage over another. France has the support of the other gold standard countries of Europe, while Great Britain takes the middle ground.

The position of France and her allies of course reflects their desire and intention to adhere firmly to the gold standard, and their view that the disorder in currencies creates a situation of special difficulty for them. That this view is well-founded has already been demonstrated in a movement of funds from Holland and Switzerland, resulting in a loss of gold by the central banks of both countries. These movements are not due to ordinary trade influences, but to the prevailing uncertainty and distrust that the situation is creating.

The cleavage runs through the conference, affecting the prospect for agreement upon measures to moderate the interferences with trade.

Aside from stabilization, the British position supports the American program. Mr. Neville Chamberlain, the Chancellor of the Exchequer, has introduced a resolution stating that "it is essential to bring about recovery in the world level of wholesale commodity prices;" that monetary action is one of the essential factors to obtain this recovery; that central banks should co-operate in a policy of cheap and plentiful money; and that central banks should coordinate open market operations in order to put available credit into active circulation.

It may be pointed out that this resolution makes no engagement on the part of Great Britain to carry out these policies pending an agreement, and goes further than British credit policies heretofore have gone. But upon the terms as stated a concord between Great Britain and this country should be easy to accomplish.

It should be emphasized, both the French and American statements agreeing, that it is not the question of ultimate stabilization and return to the gold standard which is in dispute at the Conference. All countries subscribe to that program, for the alternative is the ruinous one of a lasting disorder in the exchanges, and in all probability a competitive depreciation of currencies. Both have wrought havoc in business over the past two years.

The Agricultural Situation

The sensational rise in the price of all grains, led by wheat, has been the feature of the farm markets. It reflects a rapid change in the character of the crop reports, due to extreme heat and drought over an area which some observers estimate to include one-half to two-thirds of the acreage devoted to the major grain and feed crops. Prior to the middle of June the moisture supply and general growing conditions in the Spring wheat states and in Canada were favorable, but since then a heat wave accompanied by high winds has caused cumulative damage. With these reports piling up, the market gradually became inflamed until in the last week the forward months in the Chicago wheat market sold above a dollar for the first time in nearly three years, corn above 60 cents, and other grains at corresponding advances.

The damage to the Spring wheat crop is the more important because it follows a reduction in the Winter wheat crop to 341,000.000 bushels, the smallest figure since 1904. The average expectation for Spring wheat is around 260,000,000 bushels, and if this is materially reduced the crop will fall correspondingly short of 600,000,000, whereas the average domestic consumption for all purposes in recent years, exports not included, has been around 725,000,000. This situation has the possibilities of a great statistical improvement, and a substantial reduction in the carryover of around 350,000,000 bushels which remains from the 1932 harvest. It affords a sound basis for the price rise, and the announcement of the measures to be employed in an effort to reduce the acreage next season, under the Farm Relief Act, is another important factor.

The wheat situation in this country has been a distressing one, with the surplus mounting constantly over five years, and the mitigating factor to the losses in the drought regions is the improvement that will be worked in the situation as a whole. It is not the usual practice to welcome a bad crop, which raises the farmers' unit costs of production, gives less business along the line to the consumer, and raises the cost to the latter. However, the wheat growers for some time have been at a disadvantage, and the larger return in dollars that they receive will help to restore their position in relation to other classes of the population, more effectively than if they had produced a more abundant crop at a lower cost. The effects of the advance on the general business situation should be entirely helpful.

The Farm Relief Act

This great rise invests the provisions of the Farm Relief Act with respect to wheat with a new interest. The purpose of this act is to overcome the disparity between the prices of agricultural and non-agricultural commodities, by direct measures to reduce the production and advance the prices of the farm products. It is the theory of the Act that this disparity is a principal point of disequilibrium in the economic situation. From the start of the depression the ratio between the prices of what the farmer sells and the prices of what he buys declined, and during most of the past year it has been only about one-half of what it was in 1910-14; and of course with each unit of his production the farmer could buy only half as much of the products of other classes of the population. This is an explanation of the decline in the demand for manufactured goods, for the falling off in factory employment further reducing the demand, and so for the whole vicious circle of the depression.

Reasoning from this point the Administration reached the view that measures to increase the exchange value of farm products were necessary, and the Act gives the Secretary of Agriculture authority to carry out a variety of such measures in his discretion. In particular he is authorized to enter agreements for the allotment of production quotas to farmers, or for price-fixing; and to make "rental or benefit" payments to farmers who will contract to reduce their production. To obtain revenue for this purpose he is empowered to levy a tax on the processing of farm products. This tax will equal the difference between the current average farm prices and the "fair exchange value," which is the 1909-1914 average purchasing power of farm products with respect to articles farmers buy. In the middle of May these articles were exactly at the pre-war average, and the "fair exchange value" was therefore set at the actual 1909-1914 average farm price, or 88.4 cents for wheat, 12.4 for cotton, 7.24 for hogs, and 64.2 for corn. The tax must of course be borne by the consumer, who, however, will naturally have the option of reducing his consumption of the goods taxed if the tax is burdensome. In that case the effect will be to depress the price to the producer and thus to diminish the benefits of the plan. These provisions may be viewed as an essential part of the emergency effort to restore economic equilibrium through overhead management, and there will be a trial of them upon that basis.

The Wheat Plan

In pursuance of his authority under this Act, the Secretary has announced terms for applying these provisions to wheat and cotton, both plans contemplating payments to farmers to compensate for reduction in acreage. In the case of wheat a processing tax of 30 cents per bushel will be levied, beginning July 9, upon the millers and cereal manufacturers. This tax was apparently determined by subtracting from the 88.4 cents above given the average farm price as of June 15, which was 60 cents or slightly less. The farm price will run about 15 cents below the price in the central markets, the difference representing transportation and other costs. The proceeds of the tax will be paid to farmers who will contract to reduce their wheat acreage in 1934 and 1935 to the extent then considered necessary. The distribution will be in proportion to that part of the crop which goes into domestic consumption, and if this tax should apply throughout the crop year each farmer would receive 30 cents a bushel (less costs) on five-eighths of his average crop for the past three years. Two-thirds of the benefits will be paid September 15, 1933, the remainder when the acreage contract is fulfilled.

This tax will equal 7/10 of a cent on each pound of flour, and not more than 0.483 cent on a loaf of bread, according to calculations given in the order. The administrators of the Act are pledged to protect consumers against pyramiding of the tax through the stages of manufacturing and distribution, and the idea is prevalent that a part of the tax can be absorbed by the manufacturer and distributor without passing it on to the consumer. This idea reflects a belief that the margin upon which this business is conducted is unnecessarily wide. However, the business is as long established and competitive as any in this country, and its earnings show no margin of profit out of which any material part of a tax of $1.38 per barrel on flour can be absorbed. Moreover, the competition has probably done more to reduce costs than any fresh factor that can be brought to bear, and when these costs are analyzed it will doubtless be found that most of the items have already been deflated as much as they are likely to be under present conditions.

Effects of Price Advance on the Plan

It will be observed that a price of 90 to 95 cents for contract grades in Chicago and the equivalent 75 cents or thereabouts for the average farm price, wheat is within striking distance of the "fair exchange value" of 88.4 cents; and since it is the object of the Agricultural Adjustment Administration to put it to that price it might appear that there was little left for the Administration to do. However, its officials do not take that easy view. Secretary Wallace addressed the Millers' National Federation in Chicago on June 21, and said, referring to the small crop and the price advance:

> Of course you gentlemen know enough to know that the problem is deeper than that. You know, of course, that we still have approximately 350,000,000 bus. carry-over in prospect as of July 1 as compared with a normal carry-over of, shall we say, 120,000,000 bus. You are familiar with that.
>
> And you are also familiar with the fact that bad weather, such as we have had for this wheat crop, cannot be counted on to come two years in succession. You are aware of the fact that with wheat prices as they are today, without any type of centralized control, it would be easily possible to have such a large acreage of winter wheat planted this fall that the probabilities would be for at least an 800,000,000-bu. crop next year total, and the possibilities would be for more than a 900,000,000-bu. crop total. And, furthermore, you gentlemen know that with our relationship to the rest of the world there is not in prospect a market for the more than 200,000,000 bus. surplus, which that kind of a crop would indicate. at a price which would be high enough to make our wheat farmers a part of the American system of living.
>
> I think you are familiar with that. And it is to that problem that the Agricultural Adjustment Act addresses itself, and it is for that reason that we are so exceedingly anxious to bring about this next fall, and the following spring, and the next year, and the next year, a machinery to bring about a sufficient curtailment of acreage so that we can adjust our total wheat situation to the world situation.

This is a reasonable presentation of the situation, and is the justification for the emergency effort to accomplish the necessary readjustments by the plan outlined. It is a warning to the wheat growers that they should accede to the plan.

From this viewpoint the price rise is interpreted by the Administration as on the whole a disturbing development. It sets in motion the old conflict between the efforts of the farmers' advisors to reduce production and the stimulus of higher prices to increase production. As early as May Secretary Wallace had expressed concern as to effects of the advancing market upon the plans to cut acreage, and there is room for question as to its effects not only in retarding the acceptance of the plan, but in making the enforcement of the agreements more difficult after they are drawn.

The advance may also have been a factor in the failure to complete thus far the four-power wheat agreement in London. The United States, Canada and Argentina were ready to agree upon a 15 per cent reduction in acreage, but Australia included among other objections a grave doubt whether such a plan could be enforced, inasmuch as the agreement might cause a substantial price rise before next April, which is the Australian planting season.

Another important consequence of the rise is that it may destroy the self-financing character of the plan. Mr. Charles J. Brand, one of the administrators, is quoted as saying that the commodity price advance raises the question whether the Government will be able to collect any difference between farm market prices and the arbitrarily fixed price, for the reason that the fixed prices will have been attained. As stated, wheat has reached nearly to that point on this rise, and a calculation of the tax on the basis of today's prices, which are 15 to 20 cents higher than on June 15, would reduce it to 10 or 15 cents. There is no authority in the Act for the collection of a tax in excess of the difference between the present farm price and the "fair exchange value;" nor has there been a sufficient rise in prices of non-agricultural products to permit a revision of the "fair exchange value" upward.

Relationships to Other Industries

The foregoing description of the situation is a picture of confusing cross-currents, and shows the incalculable elements that an attempt at overhead management of agriculture has to deal with, both in nature and in the human behaviour involved. Likewise it demonstrates the tendency of efforts at such management to defeat themselves, due to the market movements in anticipation.

The fundamental question involved in the wheat plan is that of the relationship of wheat

growing to other industries. The attempt is to improve that relationship, in a time of emergency, as a measure toward restoring order in the economic system and getting the exchange of goods going again. The experimental character of the Farm Relief Act has been emphasized by President Roosevelt, who in his message transmitting it to Congress said:

> Deep study and the joint council of many points of view have produced a measure which offers great promise of good results. I tell you frankly that it is a new and untrod path, but I tell you with equal frankness that an unprecedented condition calls for the trial of new means to rescue agriculture. If a fair administrative trial of it is made and it does not produce the hoped-for results I shall be the first to acknowledge it and advise you.

Of course permanent agricultural improvement will depend upon the establishment of lasting relationships between agriculture and other industries upon the sure basis of supply and demand. In the long run neither the farmer nor any other group of producers can be assured of an income or prices fixed by law, irrespective of what happens to the rest of the community, and the artificial diversion of funds from the community in general to the farm community will add to the farm buying power only as long as the flow of funds continues. Nor will acreage readjustments bought with public money last any longer than the public money lasts. In the end the economic law will govern the distribution of the population as between farming and other occupations, and their respective returns, and planned readjustments will be permanently effective only as they are in harmony with the economic law.

The Cotton Plan

Cotton has advanced to above 10 cents in New York. The cotton situation is broadly similar to the wheat situation, but all the strengthening of the market has come from the demand side. There is an oversupply, and the carryover from this season will be around 12,000,000 bales. Moreover, the acreage planted has been increased this year by a still unknown amount, the first Government estimate being due on July 8, and growing conditions have been favorable. Mr. Brand, quoted above, is also reported as saying that unless acreage reduction plans were carried through this season cotton could go to 3 cents a pound, which would imply a lack of faith in inflation as an agency for raising this commodity.

The plan of the farm relief administration for dealing with cotton involves the imposition of a processing tax to take effect August 1, in an amount yet undetermined, but to be calculated as already described. Out of the proceeds of this tax, or if necessary other funds appropriated, growers who will plow under or mow down cotton already growing will receive cash payments ranging from $7 to $20 per acre according to the average yield of their land. Or at the grower's election he may take cash payments of $6 to $12 per acre, together with an option on an amount of Government-owned cotton equaling the crop reduction, at 6 cents a pound. The plan will take effect only if the response to the offer is satisfactory to the Department of Agriculture, which desires to take out of production as much as 10,000,000 acres.

The varying figures named for payments as compensation for not producing crops inevitably suggest the impracticability of such a policy of regulating production, as a permanent system. The average productivity of fields, and the average acreage in preceding years, must be based upon the representations of owners, subject to approval by local committees. As a means of correcting a situation which has resulted from the war, one adjustment of this kind may be worth the cost, as the only means of promptly restoring order in production, but surely more than this cannot be contemplated.

The National Industrial Recovery Act

The National Industrial Recovery Act is frankly emergency legislation, carrying extraordinary powers, for the purpose of obtaining a concentration of authority believed to be necessary for effective dealing with the disorganization existing in industry. These powers are granted under two Titles, the first devoted to a plan for the regulation of private industry and the second to a plan for inaugurating and supporting public works and construction projects under the direction of the National Government and also through loans by the National Government to state, counties and municipalities.

Under Title II a new organization known as the "Federal Emergency Administration of Public Works" will assume the function of making loans for construction purposes which heretofore has been a part of the work of the Reconstruction Finance Corporation. The scope of this Title is very broad, including, along with proposals less sweeping, authority for expenditures on behalf of the Federal Government, or loans to states, counties or municipalities, for construction work upon "any publicly-owned instrumentalities or facilities," "for conservation or control of natural resources," and "any projects of the character heretofore carried on either directly by public authority or with public aid to serve the interests of the general public." However, the loans to governments and public bodies shall not be in excess of 30 per cent of the cost of labor and materials used in aided projects, an important limitation. It is also provided that "in deciding to extend any

aid or grant to any state, county or municipality the President may consider whether action is in process or in good faith assured reasonably designed to bring the ordinary current expenditures thereof within the prudently estimated revenues thereof." The purpose of this Title clearly is to provide employment on a large scale for its effect in conjunction with the industrial control planned in Title I.

The Secretary of the Treasury is authorized to borrow from time to time, under the Second Liberty bond act as amended, such funds as may be necessary to meet the contemplated expenditures, and a sinking fund calling for 2½ per cent of the aggregate of such expenditures is established under the terms of the Victory Loan Act as amended. The act appropriates $3,300,000,000 and levies certain taxes and makes certain changes in taxation which need not be described here. The act contemplates that operations under it will terminate at the end of two years, as to the beginning of new undertakings, and earlier if the President by proclamation or the Congress by joint resolution shall declare the emergency to be ended.

Industrial Control

Although the public works program is important, interest centers upon the plan for industrial control. For, in the first place, while the $3,300,000,000 is a large sum it will have to be expended gradually, and after all is not large in comparison with the annual product of all the industries; and, in the second place, the effect of such expenditures upon the general industrial situation must depend very much upon whether or not the industries themselves are ready to move in recovery. The essential thing is to get the great, normally self-supporting, industrial organization to running again under its own power.

It is undeniable that the organization is seriously out of order. This is what makes the emergency and justifies resort to the powers granted by the act. The volume of all kinds of business has been declining heavily over the last three years, the aggregate in 1932 being scarcely more than one-half of 1929. Since in final results all business consists of an exchange of services, it is evident that the trouble is in the exchange relations. Every one buys with what he sells and although the economic system consists of a multitude of independently-owned units they must work together as a harmonious whole to have prosperity.

Professor Richard T. Ely, one of the eminent economists of this country, whose works are standard text-books, and who in a long career headed the departments of economics of Johns Hopkins and later of the University of Wisconsin, has given in two short paragraphs, first an explanation of "hard times" and then a picture of the industrial order which would produce the maximum of welfare. He says:

> As our economic life advances, it becomes more and more one of relations. When these relations are disturbed we have Hard Times. It has sometimes been said that we have now all the labor and capital, all the machinery, all the land and all the natural resources that we had during our highest prosperity in 1929; and it is argued that we are just as rich as we were before the crash, and we really ought to be equally prosperious. What is overlooked is that, as our life is one of economic relations, our prosperity depends upon the smooth and easy way in which they work. Unless these relations function properly all the other conditions of prosperity are inadequate.
>
> * * * *
>
> What we are striving for and must ever keep before us as a goal is that balanced production which giving employment to all labor, all capital and our other economic resources, would produce a maximum of satisfaction of human wants of all kinds and the nearest approach to economic felicity that human beings are capable of.

This voluntary economic system, beginning with the simple exchanges of neighbors, has increased in complexity with its development, until it is almost beyond the understanding of its members, and yet their intelligent cooperation is necessary to its successful operation. The extraordinary demands of the war-time and the violent effects of both war-time and peace-time changes have created the disorder with which all business has been struggling.

Criticisms of the Economic System

The economic system has been undergoing criticism for conditions which it did not create or have the power to prevent. It never has been a "system" in the sense of being one organization, planned and directed by an overhead authority. It has been simply a congeries of trade relations, under the authority of the political government. Moreover, the economic system has been just the kind of a system that public opinion has wanted. All of the popular struggles of the past have been to get the individual man free of overhead authority in making a living and in bargaining about his relations with other persons. The voice of the people has been for freedom of individual initiative and enterprise. Furthermore, popular opinion and the policy of the law, particularly in this country, have been against any organized efforts of business to manage or regulate production and trade. The very language, as well as the spirit, of our laws against combinations in restraint of trade have come down to us from the common law of England. The law has sought to compel competition, or at least to prevent effective cooperation among producers for suppressing even its excesses or abuses.

Abuses of Competition

That excesses and abuses have been prevalent in competition has been well known, but the economic system as a system has had little

power to deal with them. The formation of trade associations has been evidence of the desire of business men to confer upon matters of common concern and to have some rules or agreement as to what are fair business practices. In recent years under the leadership of the Federal Trade Commission, codes of fair practice have been adopted in a number of trades. Obviously such efforts are of limited scope, and can affect only those who wish to cooperate.

It has been long considered unnecessary to have agreements upon prices in order to mitigate the worst abuses of competition. The important thing is to have a common basis in fair dealing. Wages are so important a factor in industry that competitive wage-policies are the most unsettling of all means of under-cutting, and evidently wage levels should not be determined in this manner.

The increasing employment of capital in the fixed investments of industry has tended to intensify competition, by giving greater inflexibility to overhead cost, thus offering an inducement to full production regardless of market conditions. It may induce unneeded production as a means of reducing losses when there is little or no hope of profit. Such operations are demoralizing to industry and there should be some means of controlling them.

All competitive conditions are aggravated by a general depression which reduces the volume of business that can be done. The struggle for what remains is intensified and instead of policies being directed with intelligent consideration for all conditions they tend to become completely demoralized.

On the other hand, periods of general business expansion induce competitive enlargement of facilities which sometimes overload an industry with capacity when perhaps a council of the industry might lead to a more cautious policy. The great bulk of the business of this country is done upon very moderate margins of profit over an average of years, and amid changing economic conditions which involve continuing hazards to all investments. More and more the feeling has grown that honest business should have some kind of protection against unfair and destructive competition and some freedom for conference upon constructive general policies.

Modification by the Courts

Agitation for revision of the anti-trust laws has existed for years, but the chance of helpful action has seemed to be very small. The courts, faced by the practical difficulties of business as laid before them from time to time have modified the severity of the laws in some degree by reading the rule of reason into them, and an encouraging additional step has been taken recently by the Supreme Court in the Appalachian Coals Case, on appeal from the western district of Virginia. In this case 137 coal producers had formulated a plan for a joint sales agency with the frank purpose of endeavoring to modify destructive competition and establish more orderly conditions in that section of the coal industry. The district court held the plan to be in violation of law, but the Supreme Court reversed the decision and permitted the plan to go into effect on trial, the case remaining under the jurisdiction of the district court. Although this decision, which was rendered by Chief Justice Hughes is tentative rather than decisive in character, its tendency is shown by the following language:

> **Nothing in theory or experience indicates that the selection of a common selling agency to represent a number of producers should be deemed to be more abnormal than the formation of a huge corporation bringing various independent units into one ownership. Either may be prompted by business exigencies and the statute gives to neither a special privilege. The question in either case is whether there is an unreasonable restraint of trade or an attempt to monopolize.**

This is clearly suggestive that some way should be found to protect industry from ruinous disorder without compelling an undesirable consolidation of ownership. A series of decisions has shown the trend of judicial thought along this line.

This was the situation prior to the passage of the National Industrial Recovery Act. Now the entire subject of competition and industrial control is opened up for free consideration and treatment. Moreover, an opportunity is afforded for discretionary or experimental treatment in a manner that hardly would be possible under any but emergency conditions.

A Sweeping Grant of Authority

The sweeping grant of authority is tied by a declaration of policy to the provisions of the Federal Constitution giving the Congress powers to regulate interstate and foreign commerce and provide for the general welfare. A national emergency is declared to exist which is affecting commerce and the public welfare, and the purpose of the act is to promote the organization of industry for "cooperative action among trade groups, to induce and maintain united action of labor and management under adequate governmental sanction and supervision, to eliminate unfair competitive practices, to promote the fullest possible utilization of present productive capacity," etc.

The new powers are granted to the President and he is authorized to form such an organization as in his judgment will best enable him to

carry out the purposes in view. The substance of the act is in provisions for the establishment of codes of fair competition for such industrial groups as may be formed or named. The first provision authorizes the President, upon the application of such groups or associations, to approve such codes as submitted by them, provided the bodies are representative of the industries, no inequitable restrictions are placed upon membership, the codes do not permit monopolistic practices, all parties affected are given opportunity to be heard, and that he shall impose such changes or conditions as will more fully carry out the purposes in view. The next provision authorizes the President, of his own motion or in response to complaints of unfair practices, if no code of fair competition has theretofore been adopted, to take the initiative and after public notice and hearings prescribe a code which shall have the same validity as one put into effect by the method previously mentioned.

After adoption, such codes shall be standards of fair competition for the divisions of industry or trade to which they apply, and any violation of them shall be deemed unfair competition and punishable by a fine of $500 for each offense and each day that violation continues shall constitute a separate offense.

A System of Licenses

Whenever the President shall find "that destructive price-cutting or wage-cutting or other activities contrary to the policy of this Title are being practiced" he may establish in the industries so affected a system of licenses, giving notice that after a certain date no person shall engage in such line of business without a license; and the license may be revoked upon violation of the terms stated. This section of the act ceases to be in effect after one year from the date of the act, or sooner, if the President or the Congress shall declare the emergency to have ended.

For the purpose of limiting foreign competition in the domestic market, the President is authorized, if complaint is made that any article is being imported in increasing ratio to domestic production, to cause an investigation to be promptly made by the Tariff Commission, and if such representations are substantiated, to fix the only terms and conditions upon which such article may be admitted, including a limitation upon the total quantity.

The President shall afford every opportunity for employers and employes to establish by mutual agreement the standards as to maximum hours of labor, minimum rates of pay and other conditions of employment, which upon his approval shall go into effect; and where no such agreement has been arrived at, he is authorized after hearings to prescribe such code.

Every code shall contain a condition that employes shall have the right to organize and bargain collectively through representatives of their own choosing and that employes shall not be required to join company unions.

Farmers are not affected in the sale of their crops or manual laborers in the sale of their labor by any of the provisions of the act.

The petroleum industry is aided by a provision that the President may prohibit the transportation in interstate or foreign commerce of petroleum or its products in excess of the quantities that may be produced or withdrawn under state authority. The President is authorized to bring action before the Interstate Commerce Commission for further regulation of pipe line transportation charges and under certain conditions to divorce the control of such transportation from holding companies.

The provisions of the anti-trust laws are modified in whatever respect they conflict with the provisions of this act, but otherwise remain in effect. The status of the Federal Trade Commission is unchanged.

The Plan of Administration

Obviously the grant of power is extraordinary, but the undertaking would be impracticable without the concentration of authority. The intent is to restore order in industry and there is no reason to question the declaration of the President and of the Administrator, General Hugh Johnson, that they are counting upon industry to govern itself, with the Administration acting chiefly as Umpire. This would be an ideal development, for it not only would mean success in overcoming this emergency, but yield results of lasting value.

Nevertheless, with the best spirit and motive actuating all participants the regulation of industry and of competitive relations involves many difficult and important problems upon which opinions honestly differ. The situation calls for a spirit of cooperation on the part of industry, a high order of intelligence and executive ability in the supervisory authorities, and last but not least, a clear understanding of economic principles.

Not the End of Competition

There is no reason for saying that the act means the end of individualism and the beginning of state socialism. Although mention is made of "destructive price-cutting or wage-cutting," as a practice contrary to the policy of the act, there is no other suggestion of price-fixing, and it does not appear that com-

paratively low prices will be condemned so long as they do not signify unfair methods of competition. The Administrator is reported as modifying an original statement upon this point by saying that the basic codes may provide against selling below production costs, but evidently there are inherent difficulties about strict enforcement for even such a provision. Henry Ford is quoted as saying that he can not cover production costs until production is above a certain number of thousands of cars per day, and volume of production is an important factor in all industrial costs. What is to be done with products that cannot be sold above cost? It is not to be supposed that legitimate efforts to reduce production costs and thereby lower prices will be discouraged, or that there will be any attempt to regiment either wage-workers or business managers. The President has declared that "the opportunities for individual initiative will open more amply than ever."

Competition is inevitable in a free society, for it results from the public's comparison and choice among all the offerings which invite its expenditures. The desire to compete, to excel, to win a preference, is the life of all games and characteristic of human nature in all lines of effort. There is nothing degrading in honest, straightforward, effort to render the best service that can be given in any line, even though others are striving to do the same in the same line. The fundamental principle of the economic system, as indicated by Professor Ely in the second paragraph quoted above, is that there is room for all in a balanced system of production and trade, and if there is any better general method of distributing people to their places in the system than by the comparisons which are the essence of competition it has not yet been developed. It is improbable that the people of this country will place any general ban on competition or undertake to assure a profit to everybody in business.

Unity of the Industrial Organization

In the declaration of policy which begins this act, a number of worthy objects are named, but there is one which really is all-inclusive, to-wit, "to promote the fullest possible utilization of the present productive capacity of the industries." When this is accomplished it will mean that all trade is in full volume, that employment and purchasing power are restored and that products and services of all kinds are readily passing into consumption. This would be practically an attainment of Dr. Ely's goal of "balanced production," yielding a "maximum of satisfaction of human wants of all kinds." This requires a right distribution of production capacity in the various industries and occupations and a right adjustment of price relations between the various products and services, in order that the entire body of offerings may clear itself in the markets, virtually by the process of exchange.

Although a perfect state of balance is not maintainable on account of the changes always going on in industry, a remarkably close approximation has been generally maintained in what may be called normal times, i. e., when the normal activities of industry and trade were not affected by influences arising outside of themselves, as from war or speculative excitement. This approximate balance has been accomplished by the simple workings of the law of supply and demand. Personal compensation has been adjusted to the supply of and demand for services of different kinds, and the prices of products have fluctuated to suit similar conditions. This has been naturally so, because the price of a service or product affects at once both the supply and the demand. Most of the disorders in the business world have been due to efforts to evade or suppress the law of supply and demand. There is no object in producing except to supply wants, and while wants in the aggregate are practically unlimited they are relative to each other and production must be directed accordingly. The entire productive system must be viewed as one organization, with all of the parts buying from and selling to each other, and receiving their real pay in each other's products and services. If the offerings do not buy and pay for each other, surpluses will be left over with all the results we have been witnessing in the last three years.

No Danger of General Overproduction

The declaration of policy indicates a belief that complete employment of present industrial capacity can be obtained, and Dr. Ely, in agreement with practically all economists of authority, has no misgivings either as to that or the possibility of using a constantly increasing capacity. If the reader has any doubts on this score let him mentally divide the population between, say the 10 or 20 per cent having the largest incomes and the remaining 80 or 90 per cent, and ask himself if the larger division would not be glad to raise its scale of expenditures to the same level as that of the smaller division. There is no doubt about the answer, but any substantial increase in the expenditures of that proportion of the population over what they were in the five years 1925-1929 would require approximately a corresponding increase in the capacity of the industries, and could be only accomplished gradually.

This is merely to emphasize that fears of excessive productive capacity are unfounded,

provided the new organization is able to achieve the goal of balanced relations, and that while the scheme of spreading work can be justified as a means of tiding over a disordered situation, there will be no need for it when order is restored. Moreover, there is danger that minimum wage-rates fixed with reference to a short work-week may have the effect of increasing costs, and thus prove an obstacle to recovery. In so far as the argument for the short week is based upon the theory that without it full employment cannot be had for the working population, it is fallacious. The only condition necessary to full employment is balanced relationships and the Recovery Act clearly seeks to accomplish this by coordination of the industries.

The Source of Purchasing Power

Much that is said about the necessity for building up purchasing power indicates some confusion of thought on that subject. The highest volume of purchasing power obtainable from our present productive equipment will be flowing through the markets when all the industries are operating to capacity in balanced relations. The commodities themselves will constitute purchasing power, creating demands for each other and means of payment.

As has been often pointed out, much of the confusion over purchasing power arises from the fact that everything is priced in terms of money, although in order to get money it is necessary to give products or services for it. The real purchasing power is in the latter, and whenever they are thrown out of their accustomed relations there is loss of purchasing power.

Wages as Purchasing Power

Wages of course are very important in the sum total of factors which make the industrial balance. They have played an important part in the derangements that have occurred since 1914, great variations having occurred among wages in the different lines. The real test of whether wages are relatively high or low is in their purchasing power over commodities, and particularly in relation to living costs. A recent bulletin issued by the National Bureau of Economic Research, prepared by Professor Wolman of Columbia University, from data gathered by the Bureau of Labor, gives comparative figures for wages in 1929 and 1932. Reviewing seven important wage-earning groups they show that in four of them the purchasing power of the average weekly earnings of all employed persons was higher in 1932 than in 1929, while in the other three groups they were lower. The groups in which real wages were higher were railroads, public utilities, anthracite coal and wholesale and retail trade. They were lower in bituminous coal, metalliferous mining and the manufacturing group as a whole.

This showing is enough to suggest caution about a general rise of wages as a means of distributing purchasing power. The industries can distribute no purchasing power which they do not obtain from the public. Wages not only constitute purchasing power to the wage-workers but enter into the prices of industrial products and thus into the cost of living of the entire population, wage-workers included. Wages are not wholly a matter between employers and the employed; they affect the relations between the different groups of the industrial system. An increase of wage rates already above the general level of compensation would be at the expense of the workers whose purchasing power is already below that of the fortunate group, and would increase the disparity which is the very cause of the disorder. Wages like prices are comparative and must be judged by their relations to each other and to the general industrial balance.

Must Play the Game

The economic system is like any other organization in which men work or play together, in that it must be properly balanced in all its parts in order to obtain the best results. The emphasis must be on the efficiency of the organization as a whole. Every individual or industrial group is so much better off as a part of the modern economic system, with all of the specialized learning and the vast machine equipment at its command, than he or it would be without the system, that complete loyalty is owed to it. Every group has vastly more to gain through the efficiency of the organization as a whole than it possibly can gain by efforts to advance its own interests at the expense of the whole.

The new organization should be helpful in overcoming the present state of disorganization. It furnishes a meeting ground for interests which really have a common stake in prosperity, but have been accustomed to see their relationships from different angles. If they are brought to a better understanding of the economic system and their mutual obligations in it much good will be gained. It remains, however, to be seen whether this will occur or whether the seeming investment of power may not stimulate an increase of demands on the government, with "strikes," "holidays," and "marches" on Washington. After all, prosperity and progress must be gained by compliance with economic law, and the new organization will have the greatest possible degree of success if its operations are guided in close conformity to the Law of Supply and Demand.

Printed in U. S. A.

A.